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Weekly Commentary, Selected Financial Data, and Business Indicators

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A Fixed Exchange Rate System . . .

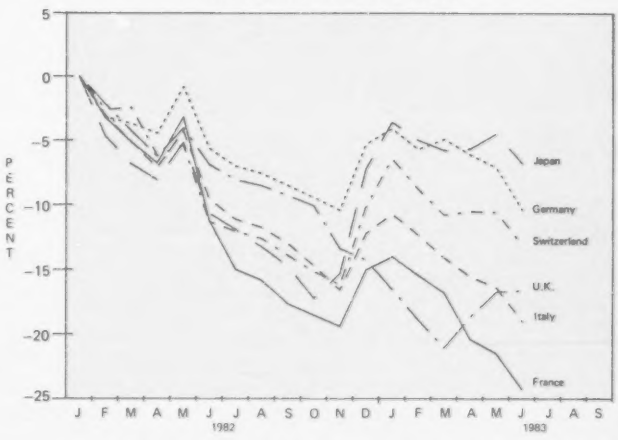
Although the call by President Mitterrand of France for a conference on the international monetary system received grudging acceptance by the participants at the Williamsburg Summit Meeting, the associated idea of a return to fixed exchange rates did not. The joint declaration at the end of the conference agreed "to consider the part which might, in due course, be played . . . by a high-level international monetary conference." The additional burdens placed on the already overburdened French economy by the persistent strength of the dollar lies behind President Mitterrand's advocacy of fixed rates.

In the three weeks which have elapsed since the end of the Summit, the dollar has continued its recent surge against the other principal trading currencies, hitting record highs against the French franc. Last week, the franc was over ten per cent below its level against the dollar in January (see chart). On a trade-weighted basis, the dollar has appreciated five per cent in the same period and is now within one index point of its high of last November.

High real interest rates, particularly long-term rates in the United States, continue to sustain the dollar. These high real interest rates are fed not only by the huge fiscal years 1982 and 1983 Federal budget deficits, but by the prospects of massive deficits in the future. These rates attract capital inflows, adding to the demand for dollars, and they undermine the confidence of business in the near-term prospects for further interest rate cuts. The sensitivity of foreign exchange rates to changes in interest rates is clearly indicated by the weakening of the dollar against the other major currencies late last year, when reductions in the U.S. discount and prime rates led foreign investors to think that interest rates were finally on their way down. The dollar again surged when the decline in interest rates stopped.

The damage done abroad by the strong dollar is widespread. In addition to investment-related capital outflows from other countries to the U.S., most international trade transactions, particularly oil prices, are denominated in dollars. Thus, the cost of imports for foreign countries rises in terms of their domestic currencies each time the dollar appreciates. At the same time, the interest cost on their dollar borrowings becomes more onerous.

VALUE IN U.S. DOLLARS OF CURRENCIES
% CHANGE FROM JAN. 1982



. . . Won't Solve The Problems . . .

In spite of the problems created by the prolonged overvaluation of the dollar, most commercial bankers, central bankers and economists agree that a fixed exchange rate system would not be viable or workable in the current economic environment. In fact, the Bretton Woods system of fixed exchange rates was workable only as long as the United States was willing and able to act as the world's banker by guaranteeing to redeem dollars for gold at a fixed price. When this guarantee was repudiated in 1973, the system rapidly fell apart.

But even under the Bretton Woods system, changes in exchange rates became increasingly frequent as the major industrial economies recovered at different rates from the effects of World War II. By the time that the Bretton Woods system finally expired, several nations, including West Germany and Japan, had again become major economic powers and were eager to play an independent role as they pursued their own economic goals.

It is the divergence of economic goals and, more particularly, economic performance, which causes exchange rates to diverge. Differing rates of inflation,

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for example, alter the purchasing power relationship between two currencies, causing the one with the lower inflation rate (and, hence, more "real" value) to rise against the other.

In the present floating foreign exchange arrangement where few restrictions are placed upon adjustments among currencies, exchange rate changes can be both large and rapid. The European Monetary System (EMS), which is an attempt by ten European countries to establish a semi-fixed currency relationship, has found it necessary to adjust its intra-system exchange rates with increasing frequency, particularly in the last 18 months, as inflation rates began to diverge widely. For example, over the past year, consumer prices in France have risen 9.1 per cent, whereas in Germany, they have risen by only three per cent. The EMS cannot long sustain such disparities in economic performance. The difficulties in maintaining stable exchange rate parities experienced by fixed, semi-fixed and floating arrangements leads to the conclusion that the system under which currencies are traded is less important than the economic environment. Fixed exchange rate systems collapse under the pressure of divergent economic performance and floating rate or semi-fixed systems (such as the EMS) become volatile and unstable.

. . . Of Divergent Economic Performance

The problems associated with returning to a fixed rate system are widely recognized. Even

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 6/8/83	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	149.448	+ .054	+10.739
Loans to Depository Inst.	.906	– .227	– .398
Float	2.195	+ .404	– .269
Total Reserve Bank Credit	160.560	+ .145	+ 9.565
Treasury Deposits with Federal Reserve Banks	2.648	– .235	– .761
Currency Outside Banks	142.671	+ .984	+11.705
Member Bank Reserves:			
Required	37.031	– .714	– 1.370
Excess (Deficiency)	.749	+ .172	+ .600
Total Reserves Held	37.780	– .542	– .770
Net Free Reserves	.403	+ .321	+ 1.226
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	110.145	+ .062	+17.610

Monetary Aggregates †		% Change Since Three Months Ago*	% Change Since Year Ago
M1	514.1	+ 13.8‡	+ 12.4‡
M2 (May '83)	2,097.2	+ 9.1	+ 13.3
M3 (May '83)	2,477.3	+ 7.7	+ 10.6
Domestic Nonfinancial Debt (1st Q'83)	4,855.3	+ 8.9	+ 9.8

†Seasonally adjusted.

*Seasonally adjusted annual rate.
‡Four-week moving average.

New York Money Market

Offering Rates 6/17/83	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	8.15%	8.25%	8.35%
* Federal Agencies	9.00	9.15	9.70
* Project Notes—Taxfree (46% Taxable Equivalent)	9.07	9.07	10.56
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	9.13	9.45	9.80

‡Finance Company Paper—Prime

5- 14 days	8.88%
15- 29 days	9.00
30- 59 days	9.00
60- 89 days	8.88
90-179 days	8.88
180-239 days	8.88
240-270 days	8.88

‡* Bankers' Acceptances

Jul.	8.90%
Aug.	8.90
Sep.	8.90
Oct.	9.00
Nov.	9.00
Dec.	8.95

‡Industrial Paper—Prime

30- 89 days	8.88%
90-120 days	8.88

†Federal Funds Effective Rate 9.05%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'83	$ 3,171	$ 3,108	$ 2,996
Gross National Product (1972 Dollars)*	1st Q'83	$ 1,486	$ 1,477	$ 1,471
Percent Change, Annual Rate	1st Q'83	2.5	– 1.1	– 5.1
Change in Consumer Prices (new series)*	Apr '83	7.2%	1.2%	2.4%
Change in Producer Prices*	May '83	3.6%	– 1.2%	0.0%
Civilian Employment (Thousands of Persons) †	May '83	99,557	99,458	99,994
Unemployment as % of Civilian Labor Force †	May '83	10.1%	10.2%	9.4%
Personal Income*	Apr '83	$ 2,679	$ 2,659	$ 2,536
Leading Indicators Composite Index (1967=100) †	Apr '83	152.4	150.7	136.0
Industrial Production Index (1967=100) †	May '83n	144.3	142.7r	139.2
Net Change in Consumer Installment Credit †	Apr '83n	$ 2.27	$ 2.58	$ 1.62
U.S. Merchandise Trade Balance †	Apr '83	–$ 4.60	–$ 3.63	–$ 0.50
Plant and Equipment Expenditures*	3rd Q'83	$306.83(a)	$302.23(a)	$315.79
Private Housing Starts (Thousands of Units)*	May '83n	1,791	1,504r	1,028
New Construction Expenditures*	Apr '83	$ 248.0	$ 246.9	$ 226.1
Total Business Inventories †	Apr '83n	$ 505.6	$ 503.2r	$ 523.4
Total Business Sales †	Apr '83n	$ 350.6	$ 348.0r	$ 344.9

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

before the Williamsburg Summit, the heads of the central banks of the United States, Japan, France and Germany at a meeting in Brussels concluded that a return to a fixed rate system, which includes the obligation of central banks to intervene in the foreign exchange markets to sustain a threatened currency, is not possible in the foreseeable future. Foreign exchange reserves can become rapidly depleted in attempting to defend an unrealistic exchange rate against market perceptions of a currency's value. Between the end of January and the end of March, France's foreign exchange reserves fell from $17.6 billion to $14.2 billion, due to heavy intervention in the foreign exchange markets in defense of the franc.

Intervention by central banks in world foreign exchange markets has not proven effective in sustaining an exchange rate which market participants perceive as being unrealistic under any exchange rate system. Hence, central banks are reluctant to commit a large portion of their reserves to this goal. Intervention, at best, buys a little time for corrective policy changes (including devaluation, where feasible) or as a method of countering "disorderly markets," that is smoothing the downward slide of a currency. It is clear that the reintroduction of a fixed exchange rate system would not resolve the current disarray in world currency markets. M

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Negotiable Time CD's Weekly Reporting Banks			
Nationwide (6/1/83)	94,332	– 802	–41,432
New York City (6/1/83)	23,098	– 310	–10,261
Commercial Paper (6/1/83)	168,729	– 901	– 7,889*

*Series redefined: Data prior to December 1, 1982, are not strictly comparable to the data reported after that date.

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (6/1/83)	214,637	+ 2,018	+ 4,812
New York City (6/1/83)	58,094	+ 1,307	– 833

Total Loans Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (6/1/83)	505,125	+ 7,779	+15,709
New York City (6/1/83)	117,945	+ 4,410	+ 3,822

Financial Markets

	Friday 6/17/83	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	9.10%	+ .16	– 4.16
180-Day Bills†	9.40	+ .14	– 4.80
Longest Bills†	9.65	+ .21	– 4.83
Recent Issues:			
10s 6/30/85 (When Issued)	10.15	NA	
10 1/4s 3/31/87	10.45	+ .09	
10 1/8s 5/15/93	10.75	– .03	
10 3/8s 11/15/12	10.78	– .09	
Municipals:			
Bond Buyer–20 Bond Index* (6/16/83)	9.38%	– .31	– 3.25
Blue List Total ($ Million)	$1,002	–$ 278	– $ 7
30-Day Visible Supply ($ Million)	$1,284	–$1,131	– $884
Total	$2,286	–$1,409	– $891
Corporates:			
Moody's Aa Composite (6/16/83)	12.08%	– .13	– 3.21
30-Day Visible Supply ($ Million)	$675	– $225	– $700
Stocks:			
Dow-Jones Averages:			
Industrials	1,242.19	+ 46.08	+ 453.57
Transportation	581.12	+ 8.18	+ 276.11
Utilities	129.06	+ 2.26	+ 22.36
65 Stocks	492.99	+ 13.51	+ 186.21
Standard and Poor's 500 Stocks	169.13	+ 6.45	+ 61.85
N.Y.S.E. Composite Index	98.00	+ 3.55	+ 36.26
N.Y.S.E. Avg. Daily Vol. for Week (000's)	100,132	+14,302	+ 51,204

* 46% Taxable equivalent 17.37%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 6/17/83	Week Ago
Overnight	9.00%	8.88%
1 month	9.38	9.50
3 month	9.56	9.75
6 month	9.75	10.00
1 year	10.00	10.31
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	11.30%	11.45%
Long Term (7 to 15 yrs.)	11.40	11.55

FOREIGN EXCHANGE SPOT RATES

New York Opening (6/17/83)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.01972	50.70
Canada	.8113	1.2326
Denmark	.1102	9.0755
France	.1309	7.6415
Germany	.3933	2.5425
Italy	.0006629	1508.50
Japan	.004189	238.73
Mexico	.006734	148.50
Netherlands	.3522	2.8393
Switzerland	.4740	2.1098
U.K.	1.5295	.6538

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